

**UNITED STATES TAX COURT**  
**WASHINGTON, DC 20217**

**PA**

DONALD W. WALLIS & KATHRYN W.	)	
WALLIS,	)	
	)	
Petitioners,	)	
	)	
v.	)	Docket No. 2412-11
	)	
COMMISSIONER OF INTERNAL REVENUE,	)	
	)	
Respondent.	)	
	)	

**ORDER AND DECISION**

Respondent determined deficiencies of \$28,713 and \$7,442 in petitioners' Federal income tax for 2004 and 2006, respectively, and accuracy-related penalties of \$5,743 and \$1,488 for 2004 and 2006, respectively, under section 6662(a).<sup>1</sup> On January 31, 2011, petitioners filed a petition with this Court. On November 6, 2012, after filing an answer, respondent filed a motion for summary judgment and attached a declaration by William F. Barry IV, and an affidavit of L. Kinder Cannon III in support.<sup>2</sup> Pursuant to the Court's Order dated December 10, 2012,

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<sup>1</sup>Unless otherwise indicated, all statutory references are to the Internal Revenue Code (Code) in effect for the years at issue, and all Rule references are to the Tax Court Rules of Practice and Procedure. All monetary amounts are rounded to the nearest dollar.

<sup>2</sup>Mr. Cannon served as General Counsel of Holland & Knight, LLP from 2000 through 2010 and has served as General Counsel (Senior) since 2010. Payments to petitioner from Holland & Knight are the subject of respondent's notice of deficiency.

Mr. Barry is counsel for respondent in this case and acted as counsel for respondent in Wallis v. Commissioner, T.C. Memo. 2009-243.

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petitioners filed an objection to respondent's motion for summary judgment and a declaration in support on January 2, 2013.<sup>3</sup> We held a hearing on respondent's motion on May 20, 2013. Following the hearing, petitioners filed on May 24, 2013, a supplement to their objection to respondent's motion for summary judgment. Pursuant to the Court's order dated May 31, 2013, respondent filed a response to petitioners' objection, as supplemented on June 18, 2013.

We have reviewed respondent's motion and petitioners' objection, and the documents submitted in support of, and in opposition to, the motion. Some of the facts have been stipulated and the stipulated facts are incorporated herein by this reference.<sup>4</sup> We are satisfied that the material facts are not in dispute, and for the reasons summarized below, respondent is entitled to a decision sustaining the notice of deficiency. Petitioners resided in Florida when they petitioned this Court.<sup>5</sup>

Respondent's motion requests summary adjudication in his favor under Rule 121. Generally, summary judgment is designed to expedite litigation and avoid unnecessary and expensive trials. Fla. Peach Corp. v. Commissioner, 90 T.C. 678, 681 (1988). Under Rule 121(b), summary judgment may be granted with respect to all or any part of the legal issues presented "if the pleadings, answers to interrogatories, depositions, admissions, and any other acceptable materials, together with the affidavits or declarations, if any, show that there is no genuine dispute as to any material fact and that a decision may be rendered as a matter of law." See Sundstrand Corp. v. Commissioner, 98 T.C. 518, 520 (1992), aff'd, 17 F.3d 965 (7th Cir. 1994).

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<sup>3</sup>We received petitioners' objection to respondent's motion for summary judgment on December 31, 2012, but due to the holiday it was not filed with this Court until January 2, 2013.

<sup>4</sup>A stipulation of facts, executed by the parties, was lodged with this Court on March 2, 2012. Upon review of the parties' submissions to the pending summary judgment motion, it was brought to the Court's attention that the stipulation of facts had not been filed. In order to facilitate the resolution of respondent's motion for summary judgment the Court directed *sua sponte* on October 31, 2013, the filing of the parties' stipulation of facts, lodged March 2, 2012.

<sup>5</sup>Kathryn W. Wallis is a party as a consequence of filing a joint return with Donald W. Wallis.

The moving party bears the burden of proving that there is no genuine issue of material fact, and factual inferences will be drawn in a manner most favorable to the party opposing summary judgment. Dahlstrom v. Commissioner, 85 T.C. 812, 821 (1985). Although facts are viewed in the light most favorable to the nonmoving party, Naftel v. Commissioner, 85 T.C. 527, 529 (1985), the nonmoving party may not rest upon allegations and denials in that party's pleadings. The nonmoving party must set forth specific facts showing that there is a genuine dispute as to any material fact. Rule 121(d); Dahlstrom v. Commissioner, 85 T.C. at 820-821.

The issues for decision are whether Wallis v. Commissioner, T.C. Memo. 2009-243, aff'd, 391 Fed. Appx. 826 (11th Cir. 2010) (Wallis I), collaterally estops petitioners from relitigating for the years in question (1) whether payments received by petitioner from his former law firm Holland & Knight were nonemployee compensation taxable to petitioner as ordinary income, and (2) whether petitioners are liable for the section 6662(a) penalty with respect to such payments.

Petitioner, a tax attorney, was an equity partner at the law firm of Holland & Knight from January 1991 through December 2002. As an equity partner, petitioner's partnership status was governed by the Holland & Knight Partnership Agreement. The partnership agreement provided that each equity partner would receive 50 "Schedule C Units" per year. Schedule C Units had a stated value of \$300 so that the units awarded each year to equity partners, including petitioner, had an aggregate value of \$15,000. The partnership agreement further provided that upon an equity partner's death, retirement, or attainment of age 68, he or she was entitled to receive the value of his interest in the partnership, consisting of (1) the amount of his or her capital account (as disclosed in the firm's books and records), and (2) the value of his or her Schedule C Units. This sum was payable in quarterly installments until paid in full.

On March 19, 2003, petitioner withdrew as a partner from Holland & Knight. Upon his withdrawal petitioner received a document from the law firm entitled "Withdrawal Benefits Analysis" (benefits due schedule) showing the amounts owed to him by Holland & Knight and the dates payments were to be made. The benefits due schedule reflected the value of petitioner's partnership interest as \$338,162, of which \$98,162 was designated as petitioner's capital account balance, and \$240,000 was designated as the value of petitioner's Schedule C Units. Beginning in 2003 and continuing into 2006 petitioner received

quarterly payments from the law firm of \$28,180, \$8,180 of which was return of his capital account and \$20,000 of which was payment for his Schedule C Units. Holland & Knight issued to petitioner, and filed with respondent, Forms 1099-MISC, Miscellaneous Income (Forms 1099), reflecting the payments for his Schedule C Units as “nonemployee compensation”.<sup>6</sup> Petitioners did not report the Schedule C Unit payments as income on either their 2004 or 2006 return.<sup>7</sup>

Petitioners in this case were also the petitioners in Wallis I. At issue in Wallis I was the proper Federal income tax treatment of Schedule C payments totaling \$80,000 that petitioner received from Holland & Knight in 2005. The parties submitted their case in Wallis I fully stipulated pursuant to Rule 122. This Court issued an opinion in Wallis I on October 27, 2009, in which we held that the Schedule C payments were “guaranteed payments” under section 736(a)(2) and taxable to petitioner as ordinary income pursuant to sections 707(c) and 61(a). See Wallis v. Commissioner, T.C. Memo. 2009-243. On August 11, 2010, the Court of Appeals for the Eleventh Circuit affirmed our decision in Wallis I. See Wallis v. Commissioner, 391 Fed. Appx. 826 (11th Cir. 2010).

Respondent argues that the doctrine of collateral estoppel precludes petitioners from relitigating the issues of whether the Schedule C payments were nonemployee compensation taxable to petitioner as ordinary income for the years at issue, and whether petitioners are liable for the section 6662(a) penalty with respect to such payments. Respondent asserts that the legal questions raised in Wallis I with respect to these issues are identical to those raised by petitioners in this case, and the only differences are the years and the amounts of tax due. Respondent contends that there has been no change in the controlling facts or the

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<sup>6</sup>The Forms 1099 issued to petitioner showed \$80,000 and \$20,000 in “nonemployee compensation” for 2004 and 2006, respectively. In their amended reply, petitioners deny, without support, that the quarterly payments designated as nonemployee compensation were in consideration of petitioner’s Schedule C Units. Respondent, on the other hand, introduced uncontroverted evidence in the form of the benefits due schedule, a Holland & Knight payment schedule, and the affidavit of Mr. Cannon to support the contention that the payments designated on Forms 1099 as nonemployee compensation were payments made by Holland & Knight to petitioner as consideration for petitioner’s Schedule C Units.

<sup>7</sup>Similarly, petitioners did not report on either their 2003 or 2005 returns any of the payments for petitioners’ Schedule C Units received in those years.

applicable law since the resolution of Wallis I. Petitioners argue that the primary issues, facts, and legal arguments raised in this case differ significantly from those raised in Wallis I.

The doctrine of collateral estoppel may be applied in Federal income tax cases. See United States v. Int'l Bldg. Co., 345 U.S. 502, 505 (1953); Commissioner v. Sunnen, 333 U.S. 591 (1948). "Under collateral estoppel, once an issue is actually and necessarily determined by a court of competent jurisdiction, that determination is conclusive in subsequent suits based on a different cause of action involving a party to the prior litigation." Montana v. United States, 440 U.S. 147, 153 (1979) (citing Parklane Hosiery Co. v. Shore, 439 U.S. 322, 326 n.5 (1979)); see also Commissioner v. Sunnen, 333 U.S. at 599-600; Popp Telcom v. Am. Sharecom, Inc., 210 F.3d 928, 939 (8th Cir. 2000); Kroh v. Commissioner, 98 T.C. 383, 401 (1992); Gammill v. Commissioner, 62 T.C. 607, 613 (1974).

In Montana v. United States, 440 U.S. at 155, the Supreme Court established a three-prong test for applying collateral estoppel that requires a court to find: (1) the issues presented in the subsequent litigation are in substance the same as those issues presented in the first case; (2) the controlling facts or legal principles have not changed significantly since the first judgment; and (3) other special circumstances do not warrant an exception to the normal rules of preclusion. In Peck v. Commissioner, 90 T.C. 162, 166 (1988), aff'd, 904 F.2d 525 (9th Cir. 1990), we stated that the "three-pronged rubric provided by the Supreme Court in the Montana case embodies a number of detailed tests developed by the courts to test the appropriateness of collateral estoppel in essentially factual contexts." Building on the Supreme Court's analysis in Montana, this Court identified five requirements that must be satisfied for collateral estoppel to apply. See Peck v. Commissioner, 90 T.C. at 166-167; see also Commissioner v. Sunnen, 333 U.S. at 599-600; Popp Telcom v. Am. Sharecom, Inc., 210 F.3d at 939; Gammill v. Commissioner, 62 T.C. at 613-615; Kersting v. Commissioner, T.C. Memo. 1999-197.

As articulated in Peck, the following requirements must be satisfied to invoke the doctrine of collateral estoppel: (1) the issue in the second suit must be identical in all respects with the one decided in the first suit; (2) there must be a final judgment rendered by a court of competent jurisdiction; (3) the party against whom collateral estoppel is invoked must have been a party or in privity with a party to the prior judgment; (4) the parties actually must have litigated the issue and its resolution must have been essential to the prior decision; and (5) the

controlling facts and applicable legal rules must remain unchanged from those in the prior litigation. See Peck v. Commissioner, 90 T.C. at 166-167. The party asserting collateral estoppel as an affirmative defense, in this case respondent, bears the burden of proof.<sup>8</sup> See Rule 142(a).

In Wallis I the parties stipulated that the entire amount of the Schedule C payments received from Holland & Knight and reported to respondent as nonemployee compensation on Form 1099 were includible in petitioners' income for 2005. The parties disagreed, however, as to the characterization of that income. Thus, in Wallis I, we stated that the primary issue for decision was "[t]he characterization (capital gain or ordinary income) of 'Schedule C Benefits' totaling \$80,000 that \* \* \* (petitioner) received from Holland & Knight \* \* \* in connection with his withdrawal as a partner".<sup>9</sup>

In this case the parties did not stipulate that the payments received from Holland & Knight and reported to respondent as nonemployee compensation on Forms 1099 were includible in petitioners' income for 2004 and 2006. Instead petitioners contend that respondent erroneously included the payments for petitioner's Schedule C Units as income includible as nonemployee compensation. Petitioners frame the issue for decision in this case as whether petitioner received from Holland & Knight nonemployee compensation during 2004 and 2006 for services rendered in the course of Holland & Knight's trade or business. Petitioners contend that "[t]his issue was not raised, addressed or determined" in Wallis I and thus collateral estoppel does not apply. We disagree.

In both Wallis I and this case, the ultimate issue presented is whether the payments received by petitioner from Holland & Knight for his Schedule C Units constitute nonemployee compensation taxable to petitioner as ordinary income. The only differences between the issues in this case and the issues in Wallis I are the dollar amounts and years in controversy. The fact that the dollar amounts in

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<sup>8</sup>As required by Rule 39, respondent affirmatively plead collateral estoppel in his answer.

<sup>9</sup>Also at issue in Wallis I was "the characterization (capital gain or return of basis) of \$32,721 that petitioner received from Holland & Knight for his capital account". In this case respondent does not raise the issue of whether certain payments designated by Holland & Knight as payments for petitioner's capital account were capital gain to petitioners.

controversy and the tax years involved in this case are different from those in Wallis I, however, does not preclude the application of collateral estoppel. See Union Carbide Corp. v. Commissioner, 75 T.C. 220, 253 (1980), aff'd, 671 F.2d 67 (2nd Cir. 1982). Petitioners' attempt at distinguishing the issues in this case and the issues in Wallis I is unpersuasive.<sup>10</sup> Accordingly, the first of the Peck requirements is satisfied.

The second and third Peck requirements are also satisfied. This Court issued an opinion in Wallis I on October 27, 2009. See Wallis v. Commissioner, T.C. Memo. 2009-243. On August 11, 2010, the Court of Appeals for the Eleventh Circuit affirmed our decision in Wallis I. See Wallis v. Commissioner, 391 Fed. Appx. 826 (11th Cir. 2010). Petitioners do not contend that a petition for writ of certiorari is pending or was timely filed with the U.S. Supreme Court. The

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<sup>10</sup>The distinction petitioners attempt to draw between the issues in this case and the issues in Wallis I is difficult to discern. Petitioners repeatedly argue that petitioner did not receive nonemployee compensation from Holland & Knight as designated on the Forms 1099 filed with respondent. Yet petitioners conceded at the hearing on respondent's motion that the payments at issue in this case were made under the same provision of the partnership agreement as the payments at issue in Wallis I. We simply cannot discern how the payments received in this case differ from the payments received in Wallis I and the relevant facts, which are not fairly in dispute, establish that they are the same type of payments.

Petitioners also appear to be arguing in part that a party cannot be collaterally estopped from relitigating an issue if the earlier issue was decided based on stipulated facts. Petitioners cite numerous cases in the supplement to their objection to respondent's motion for summary judgment including S. Bancorporation Inc. v. Commissioner, 847 F.2d 131 (4th Cir. 1988); Vallone v. Commissioner, 88 T.C. 794 (1987); Anderson, Clayton & Co. v. United States, 562 F.2d 972 (5th Cir. 1977) and Food Mach. & Chem. Corp. v. United States, 366 F.2d 1007 (Ct. Cl. 1966), to support their contention that an issue decided on stipulated facts cannot be the subject of collateral estoppel in a later proceeding. Petitioners mischaracterize the holdings of these cases. As noted by respondent, the cases cited by petitioners do not support the proposition that issues decided on the merits based on stipulated facts cannot be the subject of collateral estoppel. Instead the cases cited by petitioners support the fundamental principle that collateral estoppel only applies to issues decided by a court on their merits.

decision in Wallis I is final. See sec. 7481(a)(2)(A). Further, the parties do not dispute that petitioners were parties in Wallis I.

With respect to the fourth Peck requirement, petitioners contend that it is not satisfied “because the issues in the present case were not actually litigated, resolved and essential to the decision in \* \* \* [Wallis I]”. Again, we disagree.<sup>11</sup> Despite petitioners’ contentions to the contrary, the issue for decision in this case is whether the Schedule C payments received by petitioner from Holland & Knight and reported to respondent as nonemployee compensation are taxable to petitioner as ordinary income. The parties in Wallis I litigated whether the Schedule C payments from Holland & Knight were ordinary income.<sup>12</sup> We resolved this issue in favor of respondent and held that the Schedule C payments designated as nonemployee compensation on Form 1099 were guaranteed payments under section 736(a)(2) and taxable to petitioners as ordinary income. Accordingly, the fourth Peck requirement is satisfied.

With respect to the fifth Peck requirement, petitioners contend it is not satisfied “because the controlling facts and applicable legal rules for the present case are not the same as those \* \* \* [in Wallis I].” Except for the taxable years and amounts at issue, we find that the relevant facts in Wallis I and in this case are

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<sup>11</sup>Petitioners assert the same assignment of error in their petition in Wallis I and in this case. In Wallis I petitioners asserted that “[t]he Commissioner erred in determining for 2005 that Petitioners are required to report non-employee compensation in the amount of \$80,000”. Similarly, in this case, petitioners assert that “[t]he Commissioner erred in determining that Petitioners should have reported, as income in the form of non-employee compensation, the amount of \$80,000 for 2004 and \$20,000 for 2006”. The primary difference between Wallis I and this case is that in Wallis I petitioners stipulated that the payments received for the Schedule C Units were includible in income, but nevertheless contended that those payments were capital gain, not nonemployee compensation taxable as ordinary income. Here, petitioners make the somewhat broader contention that the payments petitioner received for his Schedule C Units are not includible in income. This distinction does not prevent the application of collateral estoppel.

<sup>12</sup>At the hearing for respondent’s motion for summary judgment, petitioners concede that their position is that the Schedule C payments are a distribution by a partnership to a retiring partner, presumably pursuant to sec. 736(b)(1). Petitioners took this same position and made the same argument in Wallis I.



identical.<sup>13</sup> Petitioners deny that the quarterly payments received in 2004 and 2006 were in consideration of petitioner's Schedule C Units and repeatedly assert petitioner did not receive nonemployee compensation as that term is used on the Forms 1099. But petitioners do not set forth any facts establishing how the payments received in 2004 and 2006 differ from the payments received in 2005. Indeed, petitioners conceded at the hearing on respondent's motion that the payments in Wallis I in 2005 and the payments in this case in 2004 and 2006 were made pursuant to the same provision of the same partnership agreement, and that the partnership agreement was not modified during the relevant years. We conclude that the Schedule C payments received in 2004 and 2006 are identical to the payments petitioner received in 2005. Because the context in which the issues of this case arise has not changed since Wallis I, normal rules of preclusion apply. See Montana v. United States, 400 U.S. at 161. Further, petitioners concede that there has not been a "change in the legal climate", see Commissioner v. Sunnen, 333 U.S. at 606, that would preclude application of collateral estoppel.<sup>14</sup> Accordingly, the fifth Peck requirement is also satisfied.

Respondent also contends that collateral estoppel bars petitioners from relitigating whether they are liable for the section 6662(a) penalty with respect to their failure to report the Schedule C payments. In Wallis I we held that petitioners were liable for the accuracy-related penalty under section 6662(a) because their failure to report the \$80,000 in Schedule C payments was not reasonable and did not show good faith. See Wallis v. Commissioner, T.C. Memo. 2009-243. The Court of Appeals for the Eleventh Circuit affirmed our decision with respect to the accuracy-related penalty. See Wallis v. Commissioner, 391 Fed. Appx. 826 (11th

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<sup>13</sup>Petitioners' objection to respondent's motion for summary judgment is riddled with relevancy objections to respondent's statement of facts. Petitioners do not, however, set forth specific facts controverting the material facts asserted in respondent's motion for summary judgment. See Rule 121(d); Dahlstrom v. Commissioner, 85 T.C. 812, 820-821 (1985). Moreover, we find petitioners' relevancy objections unpersuasive.

<sup>14</sup>Petitioners state that "[a]s to the applicable legal rules, petitioners concede that--whatever those rules may be in \* \* \* [Wallis I] and the present case, and they are not the same rules--they remain unchanged since \* \* \* [Wallis I] was decided." Because we find that the issues for decision in Wallis I and this case are identical, we reject petitioners' contention that the applicable legal rules in Wallis I and this case are not the same.

Cir. 2010). The issue regarding application of the accuracy-related penalty was fully litigated by the parties and all of the Peck requirements for estoppel are met for the reasons set forth above. Having already decided that collateral estoppel applies to bar petitioners from relitigating the issue of whether the Schedule C payments received in 2004 and 2006 were includible as ordinary income, and having received no persuasive argument why collateral estoppel should only apply to one of the two issues decided in Wallis I, we conclude that petitioners are collaterally estopped from arguing the application of the accuracy-related penalty.

Because the material facts are not in dispute and respondent is entitled to a decision as a matter of law, it is hereby

ORDERED that respondent's Motion for Summary Judgment, filed on November 6, 2012, is granted. It is further

ORDERED AND DECIDED that there are deficiencies in petitioners' Federal income tax and additions to tax/penalties due from petitioners as follows:

<u>Year</u>	<u>Deficiency</u>	<u>Additions to Tax/Penalty Under</u> <u>I.R.C. § 6662(a)</u>
2004	\$28,713.00	\$5,742.60
2006	7,442.00	1,488.40

**(Signed) L. Paige Marvel**  
**Judge**

ENTERED: **NOV 20 2013**